

BEFORE THE WASHINGTON UTILITIES AND TRANSPORTATION COMMISSION

DOCKET NO. UE-10_____

DIRECT TESTIMONY OF

RONALD L. MCKENZIE

REPRESENTING AVISTA CORPORATION

2010 MAR 31 AM 10:41
STATE OF WASH.
UTIL. AND TRANSP.
COMMISSION

I. INTRODUCTION

1
2 **Q. Please state your name, business address and present position with Avista**
3 **Corporation ("Avista" or "Company").**

4 A. My name is Ronald L. McKenzie and my business address is East 1411 Mission
5 Avenue, Spokane, Washington. I am employed by Avista as Manager, Regulatory Accounting
6 in the State and Federal Regulation Department.

7 **Q. Would you briefly describe your educational background and professional**
8 **experience?**

9 A. I graduated from Eastern Washington University in 1973 with a Bachelor of Arts
10 degree in Business Administration majoring in accounting. I joined the Company in September
11 1974. I obtained a Master of Business Administration Degree from Eastern Washington
12 University in 1989. I have attended several utility accounting and ratemaking courses and
13 workshops. I have held various accounting positions within the Company. I have served in the
14 State and Federal Regulation Department for the majority of my career with the Company.

15 **Q. Have you previously testified before this Commission?**

16 A. Yes. I have testified before this Commission in several prior proceedings.

17 **Q. What is the scope of your testimony in this proceeding?**

18 A. My testimony addresses the accounting associated with the power cost deferrals
19 under the Energy Recovery Mechanism ("ERM") approved by the Commission in Docket No.
20 UE-011595. I also explain what is contained in the monthly reports that are filed with the
21 Commission. My testimony also addresses the level of fixed costs related to the Colstrip 3 & 4
22 generating plant (Colstrip) for 2009 and the level included in base rates.

23 **Q. Are you sponsoring any exhibits?**

1 A. Yes. I am sponsoring Exhibit No. ___(RLM-2), which consists of a copy of the
2 December 2009 monthly ERM report for informational purposes, and Exhibit No. ___(RLM-3),
3 which shows fixed costs related to Colstrip.

4 II. ACCOUNTING ASSOCIATED WITH ERM DEFERRALS

5 **Q. Would you please describe the accounting associated with the Company's**
6 **ERM deferral mechanism?**

7 A. Yes. In his direct testimony Company witness Mr. William G. Johnson discusses
8 the procedure to calculate the monthly variations between actual and authorized power supply
9 revenues and expenses. The ERM deadband and sharing mechanism were modified effective
10 January 1, 2006 pursuant to Order 03 in Docket UE-060181 dated June 16, 2006. An additional
11 modification was made to the second ERM band in a rebate situation in the Multi-party
12 Stipulation and Settlement approved by Order No. 8 dated December 29, 2008, in Dockets UE-
13 080416 and UG-080417. Under the current mechanism, monthly variations are accumulated
14 until the calendar-year deadband of \$4.0 million is exceeded. Once the deadband is exceeded,
15 50% of the cumulative variation between actual and authorized net power supply costs between
16 \$4.0 million and \$10.0 million is deferred if the deferral is in the surcharge direction, and 75% is
17 deferred if the deferral is in the rebate direction. Once the cumulative power supply cost
18 variance from the amount included in base rates exceeds \$10.0 million, 90% of the cost variance
19 is deferred for future surcharge or rebate. When actual net power supply costs exceed authorized
20 costs, entries are made to record the deferral amount by crediting Account 557.28 - Other Power
21 Supply Expenses, thereby decreasing recorded power supply expenses, and debiting Account
22 186.28 - Miscellaneous Deferred Debits. If actual net power supply costs are less than
23 authorized costs in a given month, an entry is made to record the difference by debiting Account

1 557.28 - Other Power Supply Expenses, thereby increasing recorded power supply expenses, and
2 crediting Account 186.28 - Miscellaneous Deferred Debits. An accumulated debit balance in
3 Account 186.28 represents a surcharge balance, while an accumulated credit balance represents a
4 rebate balance.

5 **Q. How is interest recorded on the deferral balances?**

6 A. Interest is calculated pursuant to the Settlement Stipulation approved by the
7 Commission's Fifth Supplemental Order in Docket No. UE-011595, dated June 18, 2002.
8 Interest is applied to the average of the beginning and ending month balances in Account 186.28
9 net of associated deferred federal income tax. The Company's weighted cost of debt is used as
10 the interest rate. The interest rate is updated semi-annually and interest is compounded semi-
11 annually. The interest rate used for the period January 1, 2009 through June 30, 2009 was
12 6.547%, the Company's weighted cost of debt at December 31, 2008. The interest rate used for
13 the period July 1, 2009 through December 31, 2009 was 6.041%, the Company's weighted cost
14 of debt at June 30, 2009.

15 **Q. How are income taxes accounted for under the deferred power cost**
16 **mechanism?**

17 A. The power cost deferral entries are not recognized in the determination of taxable
18 income for federal income tax purposes. Therefore, deferred federal income taxes are recorded.
19 Account 283.28 - Accumulated Deferred Federal Income Tax reflects a credit balance of 35% of
20 the debit balances in Account 186.28. When Account 283.28 is credited, Account 410.10 -
21 Deferred FIT Expense is debited. Likewise, when Account 283.28 is debited, Account 410.10 is
22 credited.

1 **Q. In 2009 what were the amounts deferred, absorbed by the Company, and the**
2 **balance in the 2009 deferral account, Account 186.28, at December 31, 2009?**

3 A. For the 2009 calendar year actual net power costs were less than authorized net
4 power costs for the Washington jurisdiction by \$3,037,637. Since the difference between actual
5 and authorized power costs for the year was less than the \$4.0 million deadband, there was no
6 deferral for the year as a whole, and the entire difference was absorbed by the Company.
7 However, during the months of June and July 2009, there were deferral entries in the surcharge
8 direction since the cumulative differences between actual and authorized power costs exceeded
9 the \$4.0 million deadband amount in the surcharge direction for each of those months. For the
10 months of August through November there were deferral entries in the rebate direction that
11 canceled out the surcharge deferral entries made in June and July. For the year as a whole, the
12 cumulative differences between actual and authorized power costs fell within the \$4.0 million
13 deadband, and the deferral entries netted to zero. Since the monthly deferral balances were in the
14 surcharge direction during part of the year, interest was accrued on the deferral balances. The
15 balance in the 2009 deferral account at December 31, 2009 was \$29,449 (surcharge direction)
16 and consists entirely of interest for the 2009 calendar year.

17 **III. ERM MONTHLY AND ANNUAL REPORTS**

18 **Q. Would you please describe the monthly reports that the Company submits to**
19 **the Commission?**

20 A. The Company submits monthly reports to the Commission, Public Counsel, and
21 ICNU that include the monthly power cost deferral journal entries together with backup
22 workpapers and other supporting documentation. The cover letter to the monthly report contains
23 a brief explanation of the factors causing the variance between actual and authorized power

1 costs. The beginning of the month account balances, the recorded activity within the accounts,
2 and the ending month account balances are shown. The January and July reports contain the
3 supporting workpapers for the semi-annual updates of the weighted cost of debt used in the
4 interest calculations. The monthly reports also include any new power contracts of one-year or
5 longer, entered into during the month. Attached as Exhibit No. ___(RLM-2) is a copy of the
6 December 2009 report for informational purposes.

7 **Q. What are the requirements associated with the annual filing to review**
8 **deferrals?**

9 A. The Company is required to make an annual filing, on or before April 1 of each
10 year, regarding the power costs deferred in the prior calendar year under the ERM. The filing
11 consists of testimony, exhibits, and supporting documentation. Since its inception in 2002, the
12 Company has made eight such annual filings, including the present filing covering the 2009
13 calendar year.

14 **Q. What is the review period for the annual ERM filing?**

15 A. The Commission Staff and interested parties have the opportunity to review the
16 deferral information during a 90-day review period ending June 30th each year. The 90-day
17 review period may be extended by agreement of the parties participating in the review, or by
18 Commission order.

19 **Q. When was the last annual ERM filing addressed by the Commission?**

20 A. The annual ERM filing covering the 2008 calendar year was reviewed in Docket
21 No. UE-090452. Order 01 was issued in that docket on July 16, 2009, and the Commission
22 found that the power cost deferrals for 2008 were prudent.

1 Stipulation approved in Docket No UE-080416 by Order 08 dated December 29, 2008. The
2 exhibit shows that the actual Colstrip fixed costs were higher during 2009 than the amount set in
3 rates.

4 **Q. What can be concluded from the comparison of Colstrip plant fixed costs?**

5 A. Since the actual Colstrip plant fixed costs were higher during 2009 than the
6 amount set in rates, there is no reduction in fixed costs to be subtracted from the ERM deferrals
7 for 2009.

8 **Q. Does this conclude your pre-filed direct testimony?**

9 A. Yes, it does.